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Department of the Treasury

Washington, DC 20224

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PRESP-135911-09

Date:

August 03, 2012

### LEGEND:

Trust =

Authority =

State =

Dear :

This letter ruling revokes private letter ruling 200908011 (PLR-129017-08), which was issued to Authority regarding the status of Trust on October 23, 2008. In addition, this letter limits the retroactive effect of the revocation, with respect to the status of Trust, in accordance with Internal Revenue Code (IRC) section 7805(b).

Authority is a joint powers authority under State law. Authority operates a self-insurance program for State county hospitals and hospital districts. Authority established Trust to fund retiree health benefits for its employees. In a letter dated June 23, 2008, Authority requested a ruling, on behalf of Trust, that Trust's income is excludible from gross income under IRC section 115. IRC section 115(1) provides an exclusion from gross income for income that is derived from the exercise of any essential governmental function and that accrues to a state or any political subdivision of a state. With respect to the essential governmental function requirement, private interests may not participate in the organization or benefit more than incidentally from

the organization. See Rev. Rul. 90-74, 1990-2 C.B. 34. To fulfill the statute's accrual requirement, the assets of the organization seeking a ruling under IRC section 115 must be distributed upon dissolution to one or more states, political subdivisions thereof, or other organizations whose income is excludible from gross income under IRC section 115.

By letter dated October 23, 2008, the Internal Revenue Service (IRS) ruled that Trust's income is excludible from gross income under IRC section 115, because Trust's provision of retiree medical benefits to employees of Authority constitutes an essential governmental function, and because its income accrues to Authority. The IRS subsequently informed Authority (and thereby Trust) that it intends to revoke the October 23, 2008, ruling, because that ruling erroneously concludes that the essential governmental function and accrual requirements of IRC section 115(1) are satisfied. Although not reflected in the facts articulated in the October 23, 2008, ruling, additional review indicates that Trust's operations benefit private interests more than incidentally, and that Trust's income accrues, at least in part, to those private interests through Authority's inclusion of private members. Consequently, neither the essential governmental function requirement nor the accrual requirement is satisfied. Authority has since provided supplemental information opposing revocation of the ruling.

The IRS has authority to revoke an erroneous letter ruling. See Rev. Proc. 2012-1, I.R.B. 1, section 11.04. After carefully reviewing the file containing Authority's original request for a ruling on behalf of Trust, along with all subsequent correspondence, it is determined that the ruling erroneously concludes that the essential governmental function and accrual requirements of IRC section 115(1) are satisfied. Accordingly, the October 23, 2008, ruling issued to Authority regarding the status of Trust is hereby revoked.

IRC section 7805(b) provides that the Secretary of the Treasury may prescribe the extent, if any, to which any ruling or regulation relating to internal revenue laws may be applied without retroactive effect.

Section 11.04 of Rev. Proc. 2012-1 provides, in part, that if a letter ruling is revoked, the revocation applies to all years under the statute, unless the IRS uses its discretionary authority under IRC section 7805(b) to limit the retroactive effect of the revocation. Section 11.05 provides that the revocation of a letter ruling generally applies retroactively to the taxpayer for whom the letter ruling was issued or to a taxpayer whose tax liability was directly involved in the letter ruling where there has been a misstatement or omission of controlling facts, the facts at the time of the transaction are materially different from the controlling facts on which the letter ruling was based, or the transaction involves a continuing action or series of actions and the controlling facts change during the course of the transaction.

Section 11.06 of Rev. Proc. 2012-1 provides, where the revocation of a letter ruling is for reasons other than conditions listed in section 11.05, the revocation will generally not be applied retroactively provided that: (1) there has been no change in the applicable law; (2) the letter ruling was originally issued for a proposed transaction; and (3) the taxpayer directly involved in the letter ruling acted in good faith in relying on the letter ruling, and revoking the letter ruling retroactively would be to the taxpayer's detriment.

The October 23, 2008, ruling issued to Authority regarding the status of Trust is revoked because the ruling erroneously concludes that the essential governmental function and accrual requirements of IRC section 115 are satisfied where Trust's income accrues to Authority. The mistake prompting the revocation is not attributable to Trust or Authority. Accordingly, pursuant to the authority contained in IRC section 7805(b), the revocation of the October 23, 2008, letter ruling does not have retroactive effect with respect to the status of Trust.

Sincerely,

Kenneth M. Griffin  
Chief, Exempt Organizations Branch  
Office of Division Counsel/  
Associate Chief Counsel  
(Tax Exempt & Government Entities)

Enclosures: copy for section 6110 purposes